



The Pakistan Credit Rating Agency Limited

Rating Report

K-Electric Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Jun-2019	AA	A1+	Developing	Maintain	YES
31-Dec-2018	AA	A1+	Developing	Maintain	YES
14-Jun-2018	AA	A1+	Developing	Maintain	YES
30-Dec-2017	AA	A1+	Developing	Maintain	YES
12-Jun-2017	AA	A1+	Developing	Rating Watch	YES

Rating Rationale and Key Rating Drivers

Owing to pending notification of Multi Year Tariff (MYT) for the period from July 2016 onward, K-Electric Limited (KE) from time to time has obtained extension from SECP for holding AGM for 2017 and 2018. In application to Pakistan Stock Exchange dated May 28th 2019, K-Electric informed that following the withdrawal of case before the Sindh High Court, Ministry of Energy (MoE) has notified long standing MYT on May 22nd 2019 for the period of seven years applicable from July 1st 2016 to June 30th 2023. The AGM for approval of accounts for the year ended 30th June, 2017 and 30th June, 2018 to be held, with SECP's direction. Furthermore, as per the announcement in Pakistan Stock Exchange dated June 27th 2019, meeting of KE's Board of Directors will be held on July 04, 2019 to consider the Financial statements for the year ended 30 June 2017. The company lately appointed M/s. A.F. Ferguson & Co, Chartered Accountants and M/s. BDO Ebrahim & Co, Chartered Accountants as statutory joint auditors of the company for FY17. The management has represented that AGM of the company for 2017 would now be convened after the BoD meeting. In the announcement (December 24th, 2018), K-Electric has notified that they have received fresh Public Announcement of Intention from Shanghai Electric Power Company Limited to acquire up to 66.4% voting shares of K-Electric Limited. Arif Habib Limited, acting as a manager to the offer for this acquisition, had requested the extension of 90 days in making the Public Announcement of Offer which was to be made by June 23rd, 2019, and now by virtue of this extension duly approved by SECP may be made till September 21st, 2019.

Management accounts reflect sustained business and financial risk profile of the entity. However, PACRA would continue to monitor the developments and will update its rating opinion accordingly.

Disclosure

Name of Rated Entity	K-Electric Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Power(Jan-19)
Rating Analysts	Faizan Arif faizan.sufi@pacra.com +92-42-35869504



The Pakistan Credit Rating Agency Limited

K – ELECTRIC LIMITED PROFILE	
Incorporated	1913
Major business lines	Vertically-integrated power utility
Legal status	Public Limited (Listed)
Installed Capacity	2,267MW
No. of Consumers	3,223,214
Head Office	Karachi

INDUSTRY SNAPSHOT
<ul style="list-style-type: none"> ▪ Pakistan total power generation is increasing on the back of new power projects under CPEC ▪ Pakistan’s energy mix is shifting towards Gas/RLNG and coal from Furnace Oil and other expensive sources ▪ Gas fired power plants have lowest per unit cost among all fossil fuel power plants. ▪ Going forward, cheap renewable electricity will be a challenge to viability of Gas based power plants.

PROFILE & OWNERSHIP

- KE, a vertically-integrated power utility, has been in operations for over a century
- Total installed capacity of KE’s power generation plants is 2,267MW as at end-March19. KE has an arrangement with external power producers for 1,212 MW including 650 MW from the National Grids.
- The company is ~66% owned by KES Power Limited, while GoP holds ~24% stake. However, KES Power Limited is majority owned (~52%) by Abraaj Capital with the balance held by a group of investors (Al Jomiah, Saudi Arabia and NIG, Kuwait). KES Power has entered into a Share Purchase Agreement with Shanghai Electric Power Company Limited (SEP) for sale of up to 66.4% shares of KE against a consideration of US\$ 1.77bln. The transaction will close once customary closing conditions and requisite regulatory approvals are obtained.

GOVERNANCE

- The company’s board of directors comprises of thirteen directors. All the board members are seasoned professionals having interests in various sectors of the industry.
- The CEO – Mr. Moonis Alvi – is a KE veteran. He is supported by a team of experienced professionals; management quality is considered strong.
- There are currently five committees at the board level, namely (i) Audit, (ii) Finance, (iii) Human Resource & Remuneration (iv) Strategy & Projects Committee and (v) Risk Management & Safety. This ensures effective oversight of the company’s affairs and strengthening the board’s governance role.
- Lately the company has appointed A.F. Ferguson & Co, Chartered Accountants and M/s. BDO Ebrahim & Co, Chartered Accountants as external auditors. GOP has notified on 22 May 2019, Multiyear Tariff (MYT) for K-Electric for the period of seven (7) years applicable from 1 July 2016 to 30 June 2023. The audit for FY17 and FY18 is in progress and the company is expecting to hold AGM at earliest

MANAGEMENT

- The management control of the company vests with KES Power Limited, being largest shareholder.
- Mr. Moonis Alvi has been spearheading the company since being the CEO in June 2018. He has also previously served as the Chief Financial Officer of KE.
- The organizational structure of KE is divided into three main business areas, namely (i) Generation, (ii) Transmission, and (iii) Distribution. Meanwhile, support functions such as Finance, Marketing, and HR, supply chain etc. are centralized at the company level and are headed by professionals having considerable experience in their respective fields.

BUSINESS AND OPERATIONAL RISK

- KE has a registered customer base of ~3.2mln at end-March19 (FY18: ~3mln), of which 78.4% constitute residential consumers, 20.4% commercial, Industrial 1%, and remaining comprises public consumers.
- KE’s internal power generation is dependent on the gas feed and furnace oil received; supply of gas remained volatile on account of continuing gas shortages in the country. However, SSGC is supplying RLNG in addition to natural gas to mitigate this risk. The company also has a long term oil purchase agreement with Pakistan State Oil.
- A number of key projects are in progress including i) Transmission : TP-1000 under which transmission capacity is being enhanced by 1000 MVAs, ii) Generation projects amongst others include 900MW RLNG Project, coal based IPP of 700MW in which KE has an equity stake.
- Effective and timely execution of project is likely to further uplift company’s profile in medium to long term.

PERFORMANCE

- Units billed has seen growth on an annualized basis (FY18: 13,860GWh; FY17:12,981GWh). Units billed as of 9MFY19 stood at 10,207GWh.
- Recovery ratio remained stable on annualized basis (FY18: 91.05%; FY17:90.04%). However, during 9MFY19 recoveries has been improved significantly to 92.3%. Furthermore, the management is anticipating improvement in public sector recoveries on account of settlement of old recoveries from KWSB.

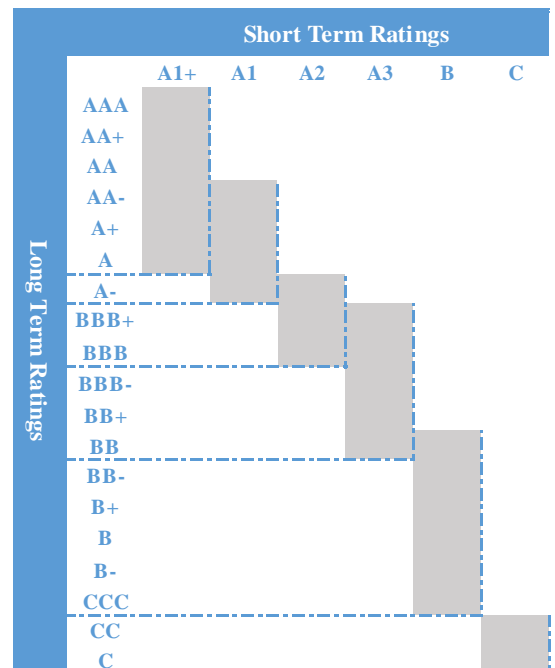
FINANCIAL RISK

- Lag in receivables is managed through combination of short term borrowings and payables.
- The company has strong cash generation ability. Cashflow stream is healthy and provides strong coverage, against liabilities. The leverage is in the comfortable range, particularly in the context of equity base. The equity base itself is strong.

Credit Rating Scale & Definitions

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
AA+ AA AA-	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	A1	A strong capacity for timely repayment.
A+ A A-	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
BBB+ BBB BBB-	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
BB+ BB BB-	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
B+ B B-	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.	C	An inadequate capacity to ensure timely repayment.
CCC CC C	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.		
D	Obligations are currently in default.		



Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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